

Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ISO-00 TRSE-00 FRB-03 NEA-14 AID-20

CIAE-00 COME-00 EB-11 INR-11 NSAE-00 RSC-01 XMB-07

OPIC-12 SP-03 CIEP-02 LAB-06 SIL-01 OMB-01 NSC-07

SS-20 STR-08 CEA-02 PA-04 PRS-01 USIA-15 INT-08 H-03

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FM AMEMBASSY LONDON

TO SECSTATE WASHDC 2247

INFO AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY THE HAGUE

AMEMBASSY TOKYO

USMISSION EC BRUSSELS

USMISSION OECD PARIS

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DEPARTMENT PASS TREASURY AND FRB

E.O. 11652: N/A

TAGS: EFIN, UK

SUBJECT: LONDON FINANCIAL MARKET COMMENTS ON ARAB FLOWS
AND EUROCURRENCY DEVELOPMENTS

REF: A) LONDON 7997; B) LONDON 6724

1. MAJOR TRENDS, REPORTED REFTEL, CONTINUE, ACCORDING TO
CONVERSATIONS DURING PAST THREE WEEKS WITH
US AND UK BANKERS. PARA 2, REF A, CITED DIFFERING RATES
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BEING BID FOR DEPOSITS. PARTICIPANTS AND OBSERVERS IN THE

MARKET ARE BECOMING INCREASINGLY AWARE OF THIS MULTI-RATE TREND. IT IS RESULTING IN PRICING PROBLEMS FOR SYNDICATED BANK LOANS. IF THE LIBO RATE (LONDON INTERBANK OFFER RATE) QUOTED TO BORROWERS REFLECTS THE LOWER BID PRICE PAID FOR FUNDS RECEIVED BY THE MAJOR INNER CIRCLE BANKS, THOSE LESS FAVORED BANKS IN THE SYNDICATE WHICH ARE HAVING TO PAY MORE FOR FUNDS WILL BE SQUEEZED. IF THE LIBO RATE REFLECTS THE HIGHER PRICE BEING PAID FOR FUNDS BY LESS FAVORED BANKS, THE INNER CIRCLE BANKS STAND TO EARN HANDSOME PROFITS.

2. THIS DILEMMA IS SEEN AS MANAGEABLE FOR NEWLY SYNDICATED LOANS, BUT CONSIDERABLE HEAD SCRATCHING AND SOME AGONIZING IS GOING ON CONCERNING HOW TO PRICE EXISTING SYNDICATED LOANS AS RATES ARE ADJUSTED ON, SAY HALF YEARLY BASIS. WHOSE LIBO IS USED? SOME OF THE EXISTING FLOATING RATE LOANS CARRY THIN MARGINS OF 1/2 TO 5/8 ABOVE LIBO. CONCEIVABLY, SOME OF ITALIAN AND JAPANESE BANKS INVOLVED MAY BE CURRENTLY PAYING AS MUCH -- OR ALMOST -- FOR THE FUNDS THEY HAVE COMMITTED AS THEY ARE EARNING ON THE OPERATIONS.

3. GENERAL POSTURE OF THE LONDON FINANCIAL COMMUNITY REMAINS DEFENSIVE AND NERVOUS, WITH FUNDS FLOWING TO THE MAJOR BANKS, AND CONSIDERABLE RELUCTANCE ON PART OF SOME INSTITUTIONS TO DEAL WITH ANY EXCEPT MAJOR NAMES. THIS IN PART STEMS FROM LEGAL UNCERTAINTIES RESULTING FROM WHAT IS TERMED THE HERSTATT FIASCO. ONE OF LARGEST CLEARING BANKS REPORTS LEVEL OF ITS FOREIGN EXCHANGE BUSINESS HAS BEEN CUT TO A THIRD. TO EXTENT THAT THIS INDICATES REDUCED SPECULATION, CLEARING BANK'S CHIEF DEALER CONSIDERS IT A GOOD SIGN.

4. WE HEAR INCREASING MARKET TALK THAT WITH HEAVY FINANCIAL FLOWS AND OPERATIONS CONCENTRATED WITH MAJOR BANKS, SMALLER ONES ARE EXPECTED TO COME UNDER INCREASING PRESSURE AND DIFFICULTY IN BUYING DEPOSITS. SOME MAJOR INSTITUTIONS OPENLY WONDER IF LONDON IS NOT OVERBANKED. AS REPORTED REFTTEL, SOME SUBSIDIARIES OF U.S. BANKS ARE ACTIVELY REVIEWING THEIR ROLE IN THE LONDON MARKET. WE CON-

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TINUE TO HEAR COMMENT THAT BANKS ARE INCREASINGLY CONCERNED ABOUT THEIR SHRINKING CAPITAL BASE IN RELATION TO INCREASED SIZE OF DEPOSITS.

5. THERE ARE UNCONFIRMED REPORTS THAT BRITISH POST OFFICE PLANS TO FLOAT \$500 MILLION EURODOLLAR ISSUE, SOME SYNDICATED FLOATING RATE MONEY TAKEN FROM BANKS, SOME LONGER TERM, FIXED RATE DIRECT FROM ARAB BORROWERS. THERE

ARE ALSO REPORTS OF ARAB, PARTICULARLY KUWAITI, INVESTMENT
IN UK REAL ESTATE AND IN TEA FUTURES.

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